

PART 1: TAX COLLECTIONS

REVENUE UPDATE

Economic growth in Utah is slowing. As a result, projected economic indicators and revenue collections are lower now than expected in February. Based on these indicators we expect General Fund revenues for FY 2008 to be close to the February target (+/- \$5 million). However, we anticipate that the Education Fund revenue will be below the February target by \$60 to \$80 million for that same year partially due to a change in income tax withholding tables. Total General and Education Fund revenues are therefore expected to be \$55 to \$85 million below February targets for FY 2008. Final balances will depend on adjustments yet to be made by the Tax Commission and the Division of Finance.

Global credit market anxiety and weak Utah home construction have contributed to the slow Utah economic growth. Growth is expected to remain stagnant with employment slowing from 4 percent in 2007 to 0.4 percent in 2008. Based upon recent research, slowdowns associated with

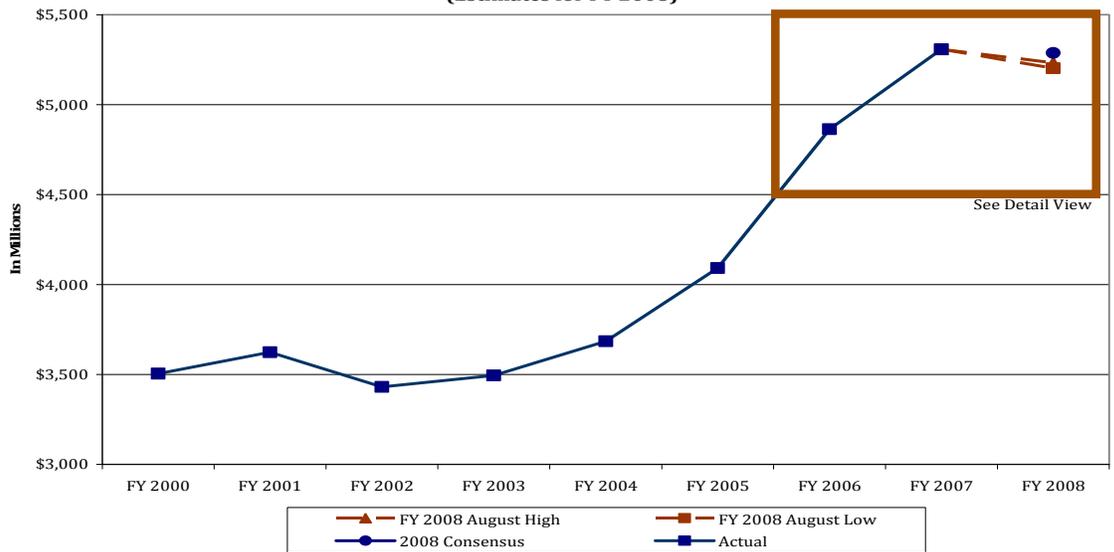
significant credit contractions tend to be worse than slowdowns with no credit contractions. This pattern is evident worldwide.

Wages continue to hold steady. However, they could potentially be outpaced by inflation in the coming year. As a result disposable income will likely decrease.

Residential construction is also expected to continue its decline. Continued strong non-residential construction growth will not be enough to offset the residential sector decline. Even non-residential construction has been adjusted down from February estimates due to financial constraints and corporate caution in expansion.

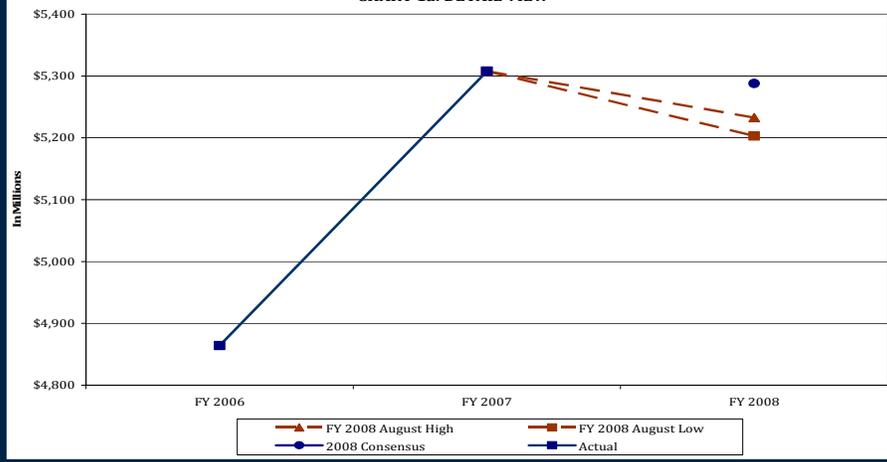
The Transportation Fund has been particularly hard hit by the economic slowdown. The decrease in vehicle miles traveled as a result of high gas prices has caused a decline in Transportation Fund revenue on both the state and federal level.

CHART 1: Combined General and Education Fund Revenue (Estimates for FY 2008)



Total General & Education Fund revenues are expected to be \$55 to \$85 million below the 2008 Consensus revenue target established in February 2008.

CHART 1a: DETAIL VIEW





GENERAL FUND

Inflation, Construction Declines & Lending Restrictions Lower Sales Tax Collections

Sales tax collections are coming in below forecasts. Among the reasons for this are inflationary pressures, construction declines, and restrictions in lending.

Sales tax collections have also been affected by earmarking and general sales tax reductions. Mortgage equity withdrawals and subprime lending have contributed to the growth in retail sales in recent years. As the spending from these sources has likely reached a plateau for the short future, sales tax revenue has and likely will continue to experience the effects.

Mortgage Equity Withdrawals have Increased Since 2003—from \$830/Person in 1998 to \$5,060/Person in 2007

It appears that individuals have used mortgage equity withdrawals as another source of spendable income. Since the first quarter of 2003, mortgage equity withdrawals have increased on an average annual basis of 6.4 percent, albeit with the latest number coming in at about half that growth rate. On a real, per capita basis, mortgage equity withdrawals have grown from \$830 per person in 1998 to \$5,060 per person in 2007.

Another explanation for slowing general fund revenue is earmarking. Earmarking in 2006 amounted to \$116 million, increasing to \$350 million in FY 2008. Adjusting for rate, base, and earmark changes, taxable sales would have increased slightly more than 2 percent

over the previous fiscal year; while unrestricted sales tax is down 5.8 percent over the previous year.

Other sources of General Fund revenue remain strong. Severance Taxes, Investment Income and Cable and Satellite Taxes have been coming in consistently above targets. Severance taxes continue to grow due to strong production and price pressure on oil and gas.

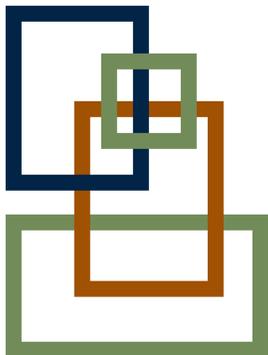
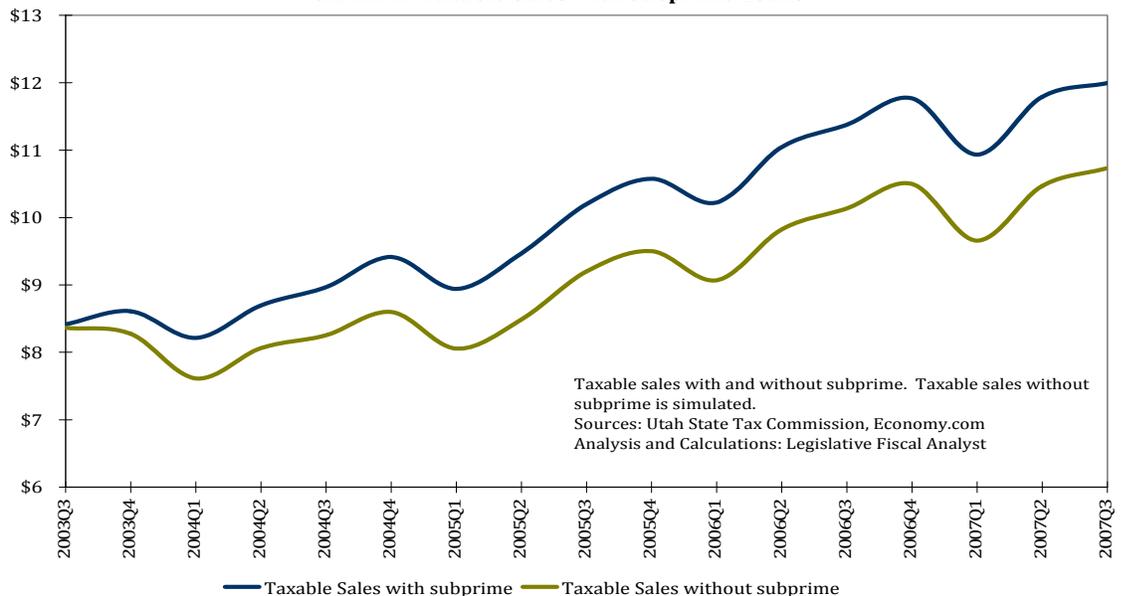
The combined General Fund revenue is expected to be close to estimates for FY 2008 +/- \$5 million.

TABLE 1: Earmarks

FY 08 Prelim.

Dedicated Credits:	
DNR Watershed Rehab./Cloud Seed	\$650,000
DNR Plants/Animal Protect.: Sales	2,450,000
Water & Wastewater - DWR	734,902
General Fund Restricted:	
Water & Wastewater Projects	23,646,793
Transportation Fund Restricted:	
Transportation Projects	29,774,963
Public Transit Systems Highway	20,855,242
Centennial Hwy 1/64 Sales Tax & Transfers (8.3 % of GF Sales Tax)	180,209,451
Critical Need Highway Fund	90,000,000
State Sales & Use Tax - Earmarked	\$348,321,350

CHART 2: Taxable Sales with Subprime Loans



EDUCATION FUND

In February of this year, the State Tax Commission changed withholding tables. Due to this change, there has been a shift forward in time of revenue from withholding to final payments. This has led to about a \$63 million dollar loss in revenue for fiscal year 2008. This revenue is recouped in January of 2009, but the withholding that would have occurred in FY 2009 has been shifted forward to FY 2010, etc., making the \$63 million a one-time FY 2008 decrease.

Wages represent the largest portion of taxable income in the state; smaller factors are capital gains, taxable pensions and interest income. Even if wages continue to hold, there now appears to be downward pressure on capital gains and interest income.

Revenues will continue to show adjustments for tax changes implemented. The next round of adjustment begin in January of 2009.

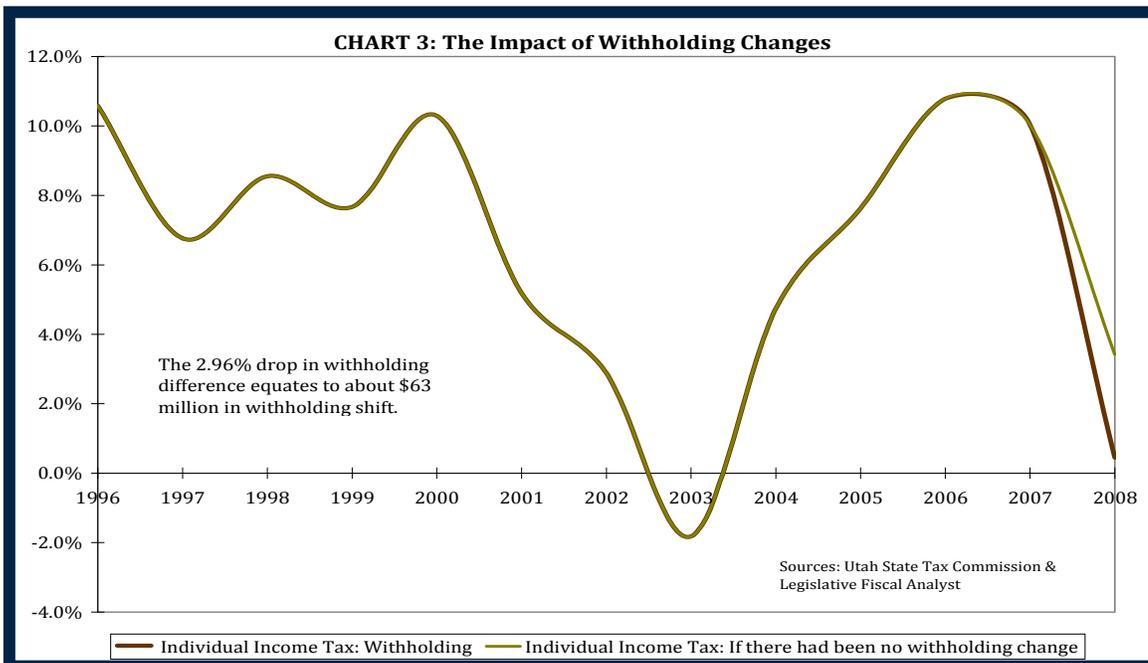
Corporate tax collections exceeded expectations in FY 2008. This is partially the result of companies relocating or expanding in Utah and

also due to an increase in prepayments and less depreciation claimed than originally anticipated. Corporate profits represent the more volatile portion of the two main funding sources for the education fund. Because of the continued strength in the manufacturing, mining, and business services, corporate profits remain stable. Corporate profits in the financial services industry, retail trade, and construction will likely be down for the coming fiscal year.

The combined Education Fund revenue is expected to be below February estimates by \$60 to \$80 million for FY 2008—final adjustments by the Utah Tax Commission and the Division of Finance may slightly modify this range. Underestimates are the result of employment changes and additional changes to the withholding tables resulting in reductions to anticipated income tax revenue.

Employment Declines and Tax Changes Reduce Education Fund Revenues

Corporate Tax Collections Exceeded Expectations in FY 2008



Changes in Withholding Tables Causes a \$63 Million Loss in FY 2008



TRANSPORTATION FUND

Consumer Behavior is Impacted by High Gas Prices

Recent evidence suggests that consumers are not viewing the run up in gasoline prices as transitory, but rather as permanent. As such, behavior is beginning to change.

Across the U.S. drivers are cutting back on mileage traveled. At the same time gas prices are at record levels. As motorists cut back on their driving and buy more fuel-efficient cars, the government is taking in less money from the state and federal gasoline tax. As motor fuel revenues decline the federal government may struggle to meet its obligations to the states placing additional pressure on state transportation programs.

Total Vehicle Miles Traveled Declines for the 9th Consecutive Month

Vehicle miles traveled on the nation's roads fell in May by 3.7 percent compared to May 2007, making May the seventh consecutive month of year-to-year decline, and the ninth in the last 12. Historically, miles traveled have risen by 1 percent to 2 percent a year.

A number of factors have contributed to the oil price increase, such as worldwide demand growth with limited supply, the exchange rate depreciation, the federal funds target rate, and

speculation. The effect of these factors on motor vehicle tax revenue is listed in Table 2. Overall, it appears that speculation is the largest contributor—absent speculation, revenue from motor fuel would have been about \$16 million more.

The Transportation Fund is also affected by slowing business activity, the byproduct of which is the demand for trucking services. Evidence suggests that both trucking tonnage and airline activity is slowing. The growth rates of these indicators are either flat or negative. This is reflected in the FY 2008 revenues, and is likely to be reflected in the coming fiscal year.

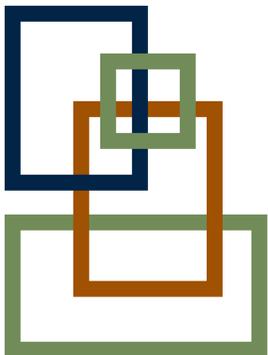
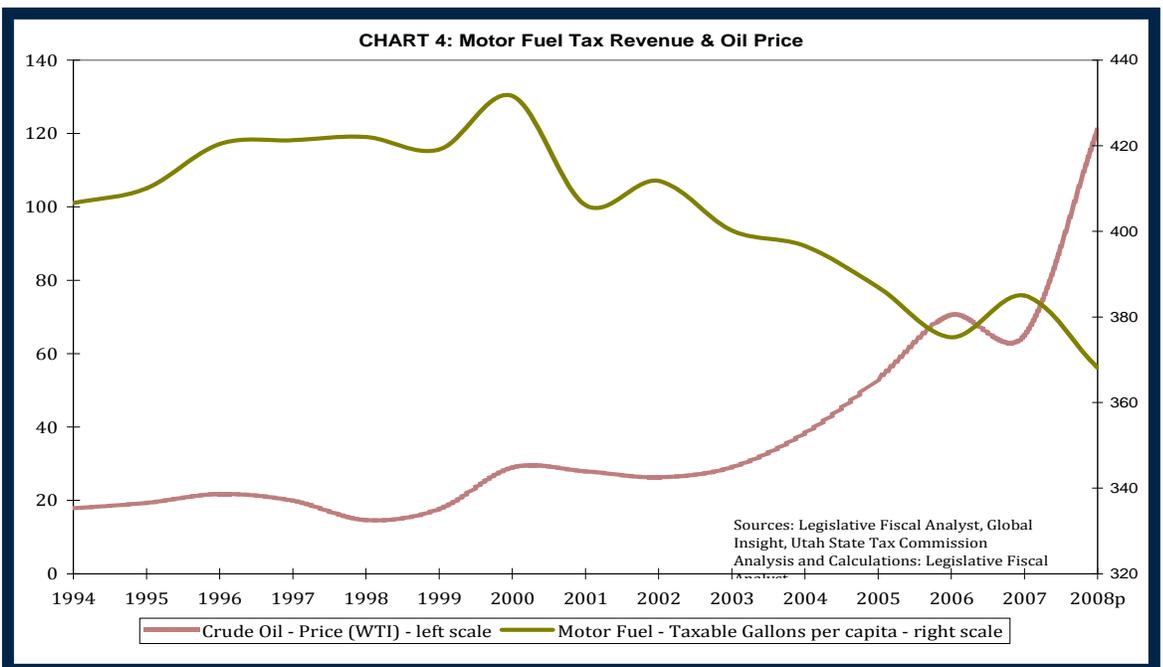
TABLE 2: Lost Revenue Due to Chinese consumption, exchange rate depreciation, speculation, and the federal funds effective rate

Fiscal Year	Factor				Total Fiscal Year
	China	Exchange Rate	Speculation	Federal Funds	
2006	(\$629,356)	(\$194,358)	(\$4,622,607)	\$574,863	(\$4,871,459)
2007	(983,956)	(712,477)	(10,015,650)	590,508	(11,121,574)
2008	(1,397,265)	(1,424,527)	(16,179,126)	(178,978)	(19,179,896)
Total Rev. Loss	(3,010,577)	(2,331,362)	(30,817,383)	986,393	
Sum Total				(35,172,929)	(35,172,929)

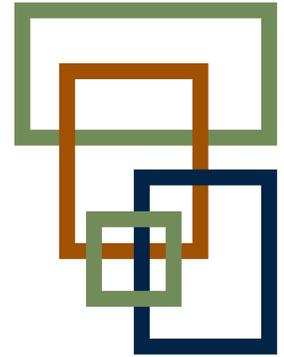
Absent these factors, revenues would have been: 781,000,929
 Total Motor Fuel Tax Revenue (FY 2006-FY 2008e): 745,828,000

Sources: EIA, IEA, Global Insight, Economy.com, Federal Reserve, Goldman Sachs, Bloomberg, CFTC Commitments of Traders CIT Supplement, Master Capital Management

Analysis and Calculations: Legislative Fiscal Analyst



PART 2: ECONOMIC INDICATORS



WAGES & EMPLOYMENT

Utah's Employment Situation: June 2008, from the Department of Workforce Services, indicated a continued deceleration in job growth in Utah. During the last revenue slowdown, jobs losses occurred in most sectors, the largest of which were leisure & hospitality, education & health, other services, and information. So far, all these sectors appear to be reasonably insulated, either due to a depreciated dollar, demand due to demographics, or other niche service. Currently, the labor market is experiencing difficulty in the construction and financial activities sectors.

Construction jobs have fallen by almost 11,000 jobs between June 2007 and June of this year. Recent estimates of the change in Utah's wage rate are 3.5 percent in 2008 and 3.0 percent in 2009. Given food and fuel inflation, all prices are expected to increase by 4 percent. Consequently, real income will fall.

The deceleration in Utah job growth will soon lead to no growth at all. Recently the Revenue Assumptions Committee forecast job growth for the state at 0.4 percent in 2008 and

1 percent in 2009. These number may prove to be optimistic. The deceleration has been led by the loss of construction jobs—especially in residential construction. Given financial problems in the banking industry and the tight credit that has resulted, we do not expect to see a rebound in the housing industry before the middle of 2009.

Conversely, Utah outpaces the nation in job creation. Utah's unemployment rate is at 3.2 percent vs. 5.5 percent nationally.

Job Growth Forecast at 0.4 Percent in 2008 & 1 Percent in 2009 may Prove too Optimistic

Job Growth in Utah Continues to Decelerate—Especially in the Construction & Financial Activity Sectors

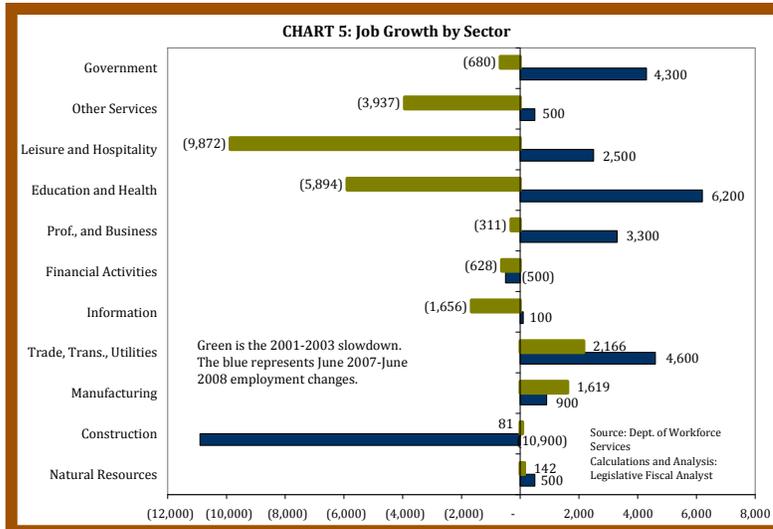
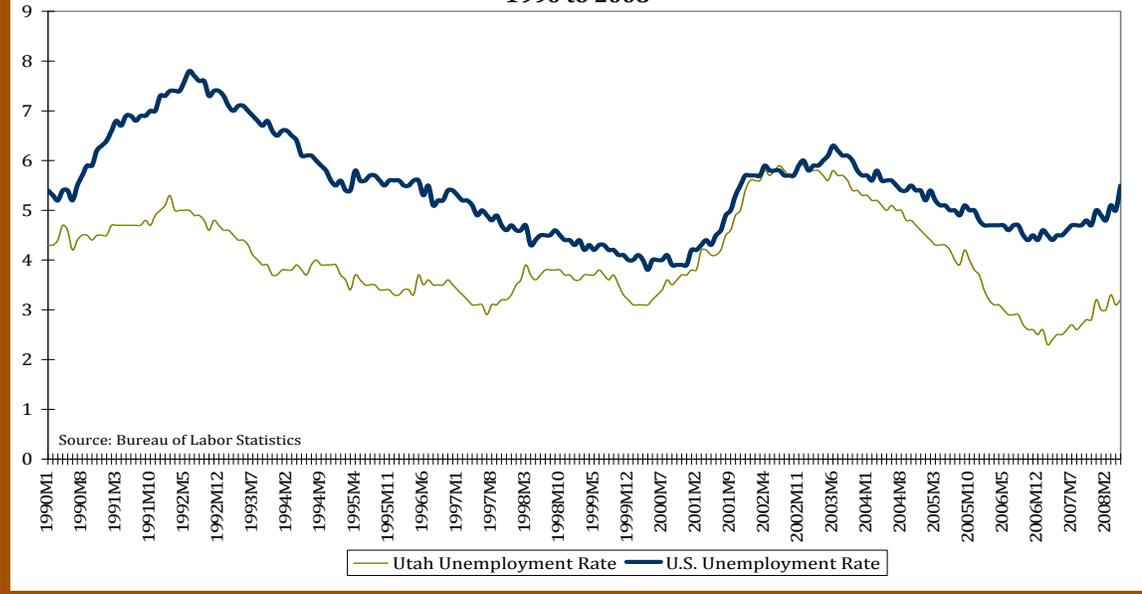


CHART 6: Unemployment Rates Utah & U.S. 1990 to 2008



Utah Outpaces the Nation in Job Creation & Unemployment in Utah is 3.2 Percent Compared to 5.5 Percent Nationally



Higher Food Prices Affect Consumer Spending—CPI for Food rose 3.9% in 2007 and Forecast to Increase to 4.9% in 2008

Food prices as measured by the CPI for Food index have increased on average 2.5 percent per year over the past 9 years. In 2007 the CPI for Food index rose 3.9 percent and it is forecast to increase 4.9 percent in 2008 (almost double the rate of growth for the past 9 years). Cereals and bakery products (grain based products) and fats and oils lead the surge in food price inflation with price increases more than 10 percent each so far in 2008.

Less Discretionary Household Income Due to High Gasoline & Food Prices may Impact Sales Taxes

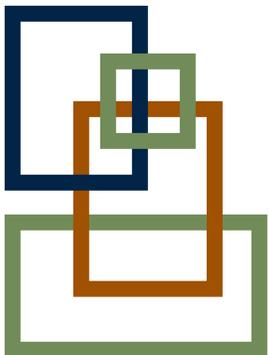
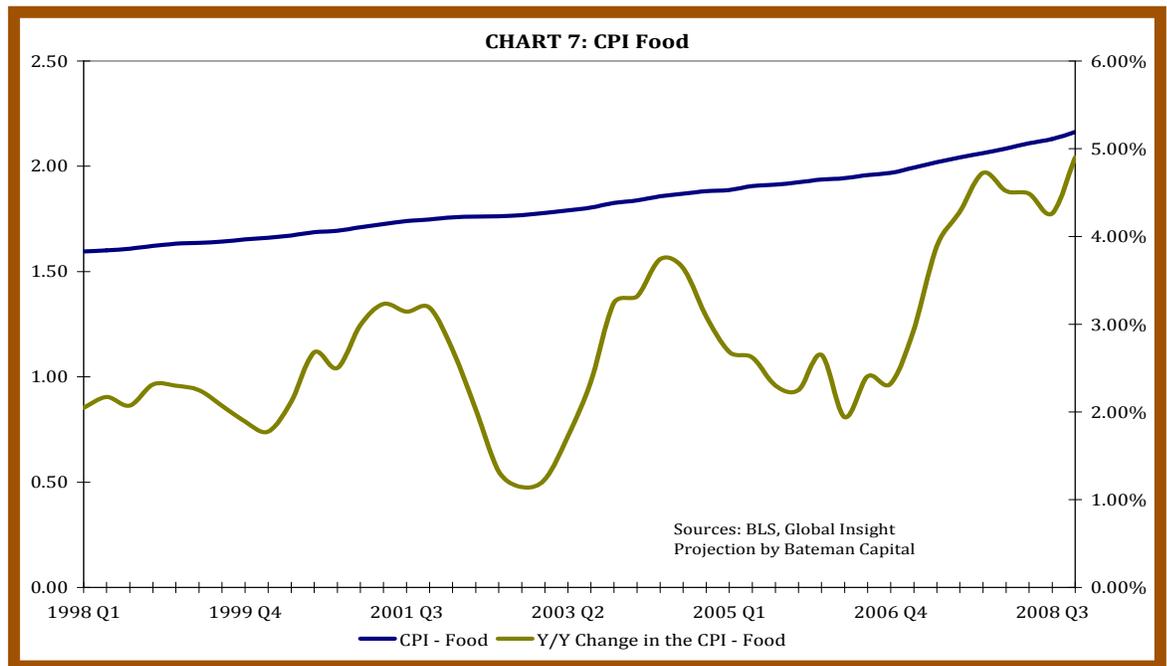
With crude oil prices trading as high as \$147 per barrel, retail gasoline prices above \$4 per gallon, and overall food prices increasing at an average rate of nearly 5 percent, the state can anticipate the following potential impacts on tax revenues:

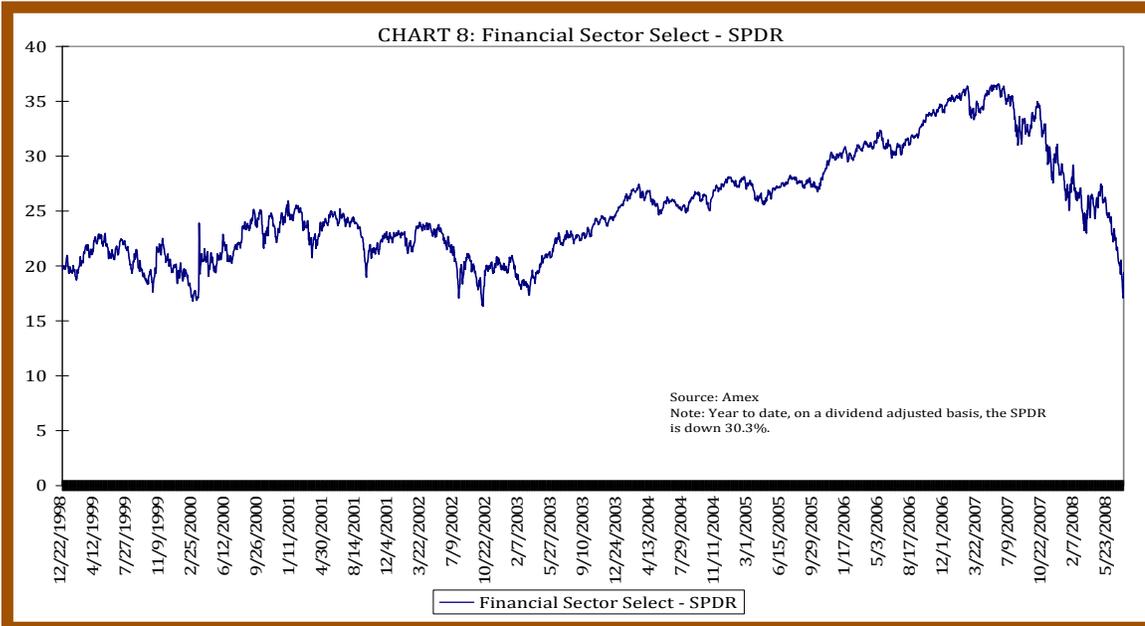
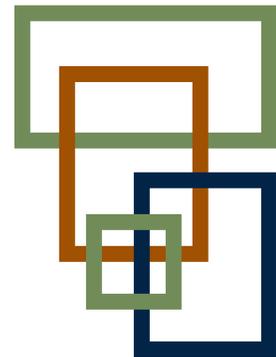
1. with a higher percentage of household income being devoted to gasoline and food due to higher prices, less discretionary income will be available for other retail purchase. This could have a negative impact on sales tax collections.

2. as higher gasoline prices begin to reduce motor fuel consumption, motor fuel tax collections will decline.
3. higher oil and natural gas prices will lead to higher production which should lead to increases in severance tax collections.

One sector, in addition to construction, in which job losses have occurred, is the finance industry with a loss of 500 jobs in Utah. Stock prices for most financial service sector companies have fallen dramatically since the beginning of 2008.

Higher default rates on sub-prime and other adjustable rate mortgages made to higher risk borrowers has led to a U.S. housing bubble, which has burst. Many banks have been reluctant or even incapable of capital creation due to significant loan losses and depletion of capital reserves as asset values have been written down. Tighter credit is placing downward pressure on economic activity. (See CHART 8 on page 7).





Stock Prices for most Financial Service Sector Companies have Fallen



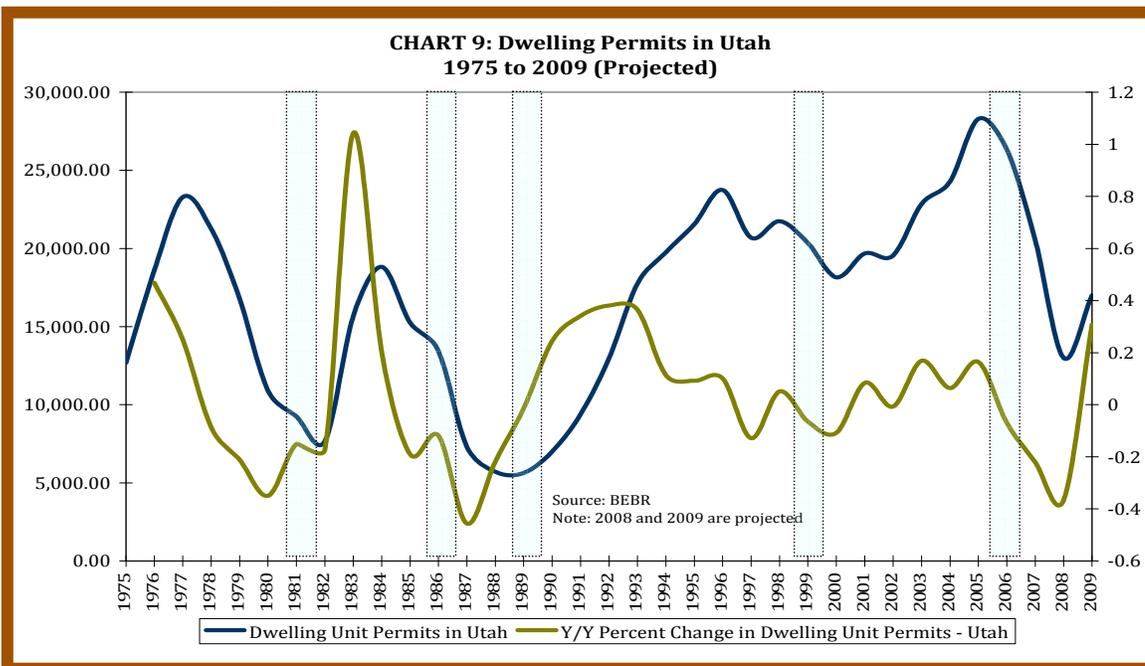
RETAIL & CONSTRUCTION

As home inventories grow, Utah and the U.S. have seen significant reductions in new home construction and home prices. U.S. housing starts are forecast to drop below 1 million in 2008. This will be the lowest figure recorded since 1959. Utah dwelling unit permits are forecast to be 13,000 in 2008, less than half the 2005 total of 28,300 and the lowest level of home building in Utah in more than 10 years.

Lenders are now more cautious, credit standards have been tightened, and home equity is no longer a reliable credit pool.

By the end of August, the Federal government will have sent about \$900,000,000 to Utah residents via tax rebate checks. Originally, estimates indicated that about 80 percent of this would be spent on taxable goods. It appears that this might have been optimistic. We won't know the exact number for a few months, but initial estimates indicate that in the aggregate consumers may have spent as little as 50 percent of their respective stimulus checks on consumption increases.

U.S. Housing Starts are Forecast at Below 1 Million—Lowest Since 1959



Utah Dwelling Unit Permits to be 13,000 in 2008—Lowest Level of Home Building in 10 Years



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CONTRIBUTORS:

JONATHAN C. BALL
 DIRECTOR

DR. ANDREA WILKO
 CHIEF ECONOMIST

DR. THOMAS YOUNG
 ECONOMIST

REVENUE COLLECTIONS TO DATE (12 MONTHS)

Major Tax Sources (In Millions of Dollars)	FY 2007 Final	FY 2008 February Consensus (2/12/2008)	FY 2008 February Growth Rate	FY 2007 Year-to-Date (7/9/2007)	FY 2008 Year-to-Date (7/8/2008)	FY 2008 Year-to-Date Growth Rate
Sales & Use Taxes	\$1,857.81	\$1,795.38	-3.4%	\$1,854.13	\$1,749.28	-5.7%
Individual Income Tax	2,570.45	2,708.90	5.4%	2,577.27	2,597.30	0.8%
Corporate Franchise Tax	427.96	382.21	-10.7%	434.48	428.33	-1.4%
Beer, Cigarette & Tobacco	62.41	66.86	7.1%	62.63	65.62	4.8%
Insurance Premium Taxes	71.78	76.76	6.9%	72.31	77.54	7.2%
Severance Taxes	89.03	80.11	-10.0%	99.46	100.36	0.9%
Total - General & Education Funds	\$5,079.44	\$5,110.22	0.6%	\$5,100.28	\$5,018.43	-1.6%
Motor Fuel Tax	\$254.68	\$265.85	4.4%	255.60	250.72	-1.9%
Special Fuel Taxes	111.17	121.29	9.1%	112.60	115.37	2.5%
Motor Vehicle Registration Fees	34.29	35.35	3.1%	34.95	36.06	3.2%
Total - Transportation Fund	\$400.14	\$422.49	5.6%	\$403.15	\$402.15	-0.2%

Source: Utah State Tax Commission, TC-23 Report.